

IRS News Release

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IRS Issues Guidance on Recoverable Reserves

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WASHINGTON — The Internal Revenue Service today issued new guidance on the computation of total recoverable units for purposes of computing cost depletion under Section 611 of the Internal Revenue Code. This guidance was developed under the Industry Issue Resolution program (IIR).

The IRS issued Revenue Procedure 2004-19, which provides an elective safe harbor where an owner of domestic oil and/or gas properties may use an estimate of the properties' "probable" or "prospective" reserves for purposes of computing cost depletion under

Section 611 of the Code. The safe harbor contained in the Revenue Procedure allows taxpayers and the Service to avoid complex factual arguments over what constitutes the appropriate quantity of probable or prospective reserves for purposes of computing cost depletion. Under the safe harbor, the IRS will not disturb a taxpayer's estimate of an oil and/or gas property's total recoverable unit where that estimate is equal to 105 percent of the property's proved reserves as defined in 17 C.F.R. Section 210.4-10(a) of Regulation S-X, remaining as of the taxable year.

It is estimated that for 50 percent of the taxpayers having a primary business of oil and gas extraction, cost depletion comprises a substantial portion of their depletion deduction. The safe harbor contained in Revenue Procedure 2004-19 will reduce the burden for electing taxpayers by eliminating the need to determine probable and prospective reserves solely for computing cost depletion for tax reporting.

The IIR Program, launched in 2001 by the IRS, tackles tax issues submitted by taxpayers, associations and other groups representing businesses. The objective is to resolve frequently disputed or burdensome tax issues more efficiently.

As part of the IIR Program, business taxpayers are encouraged to submit tax issues they believe could be resolved more efficiently with new or improved guidance. Submissions received are reviewed semi-annually – with selections next being made from issues submitted by March 31, 2004.

Revenue Procedure 2004-19 will be in Internal Revenue Bulletin 2004-10, dated March 8, 2004, and will be posted on the IRS Web site, irs.gov. Information on the IIR Program is found in Revenue Procedure 2003-36, also available at the Web site.